92-34

No. _____

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1991

MUSICK, PEELER & GARRETT, LEONARD CASTRO, ROBERT SCHUCHARD, J.H. COHN & CO., ED BACANI and ROBERT TORKAR,

Petitioners,

vs.

EMPLOYERS INSURANCE OF WAUSAU and FEDERAL INSURANCE COMPANY,

Respondents.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether federal courts may imply a private right to contribution in Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 of the Securities Exchange Commission?

PARTIES TO THE PROCEEDING

The parties to the proceeding in the court below are those named in the caption, K.M.G. Main Hurdman and Peat Marwick, Main & Co.

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No. _____

In The

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MUSICK, PEELER & GARRETT, LEONARD CASTRO, ROBERT SCHUCHARD, J.H. COHN & CO., ED BACANI and ROBERT TORKAR,

Petitioners,

vs.

EMPLOYERS INSURANCE OF WAUSAU and FEDERAL INSURANCE COMPANY,

Respondents.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

Petitioners, Musick, Peeler & Garrett, Leonard Castro, Robert Schuchard, J.H. Cohn & Co., Ed Bacani and Robert Torkar respectfully pray that a writ of certiorari issue to review the decision of the United States Court of Appeals for the Ninth Circuit, dated January 23, 1992, which appears in the Appendix at App. 1.

The decision reversed the district court's dismissal of this litigation on the ground that the plaintiff insurance companies may assert a private right of contribution under section 10(b) of the Securities Exchange Act of

1934. The insurance companies made their claims as alleged subrogees of defendants who settled a securities class action before the insurance companies filed this action. The Ninth Circuit based its decision on its rule that section 10(b) and rule 10b-5 of the Securities Exchange Commission "imply a right of contribution." *Smith v. Mulvaney*, 827 F.2d 558, 561 (9th Cir. 1987). App. 4. The Ninth Circuit's rule conflicts directly with the Eighth Circuit's holding that federal courts lack the power to imply such a right of contribution in the same provisions. *Chutich v. Touche Ross & Co.*, 960 F.2d 721 (8th Cir. 1992), *reh'g en banc denied*, 1992 U.S.App. Lexis 10390 (8th Cir. 1992).

OPINIONS BELOW

The Opinion of the Ninth Circuit appears in the Appendix at App. 1. The opinion is reported at 954 F.2d 575.

The decision of the District Court appears in the Appendix at App. 14. The decision is reported at Fed.Sec.L.Rep.(CCH) ¶ 95208.

The Judgment of the District Court appears in the Appendix at App. 31. The Judgment is unreported.

The order of the Ninth Circuit denying rehearing and rejecting the suggestion of rehearing *en banc* appears in the appendix at App. 32. The order is unreported.

JURISDICTIONAL STATEMENT

The decision of the Court of Appeals was entered on January 23, 1992. A timely petition for rehearing with suggestion for rehearing *en banc* was denied on May 28, 1992.

Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j, provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange –
>
> (a) . . . .
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5 of the Securities Exchange Commission, 17 C.F.R. § 240.10b-5 provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

The *Cousins* Case.

Certain individuals in 1984 filed a securities class action denominated *In re Cousins Securities Litigation*, No. 84-1821-B(IEG) in the United States District Court for the Southern District of California. Defendants in the case consisted primarily of Cousins Home Furnishings, Inc. and its directors and officers. After extensive discovery, the *Cousins* case was settled for $13,500,000, of which Employers Insurance of Wausau and Federal Insurance Company paid all but $500,000. In the course of obtaining court approval of the settlement, the insured defendants made extensive representations that they were paying their "fair share" of the total damages sustained by the class. Judgment was entered dismissing the *Cousins* case pursuant to the settlement on August 23, 1988.

Parties to Respondents' Lawsuit.

Respondents, Employers Insurance of Wausau and Federal Insurance Company, provided insurance to certain of the defendants in the *Cousins* case. Petitioners are attorneys, accountants and their firms. Petitioners provided professional services to the *Cousins* defendants during the time defined as the class period in the *Cousins* case.

Respondents' Lawsuit.

Respondents sued Petitioners for damages approximately eight months after the *Cousins* case concluded. Respondents allege they are subrogated to the rights of

the defendants in the *Cousins* case whose settlement Respondents funded. Respondents assert claims for contribution under state and federal law, including section 10(b) of the Securities Exchange Act of 1934 ("the Exchange Act") and Rule 10b-5 of the Securities Exchange Commission, 17 C.F.R. § 240.10b-5 ("Rule 10b-5"). The District Court had jurisdiction pursuant to 28 U.S.C. § 1331.

The District Court granted Petitioners' motion to dismiss Respondents' lawsuit. Judgment of dismissal was entered April 12, 1990. Respondents appealed.

The Ninth Circuit Decision.

The Court of Appeals reversed the District Court in a published opinion. The Court of Appeals acknowledged neither section 10(b) of the Exchange Act nor Rule 10b-5 provides an explicit right of contribution. The Court of Appeals reaffirmed its rule implying a private right of contribution in section 10(b) and Rule 10b-5.[1] *Smith v. Mulvaney*, 827 F.2d 558, 561 (9th Cir. 1987). The Ninth Circuit went on to rule that settling defendants' representations that they paid their "fair share" of damages did not waive or bar their claims for contribution.

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[1] The Ninth Circuit firmly enforces a rule forbidding any three judge panel from overruling a previous Ninth Circuit panel decision. *United Scottish Ins. Co. v. United States*, 614 F.2d 188, 191 (9th Cir. 1980); *Pratt v. McCarthy*, 850 F.2d 590, 593 (9th Cir. 1988); *Hard v. Burlington Northern Railroad Co.*, 870 F.2d 1454 (9th Cir. 1989); *Owen v. Commissioner of Internal Revenue*, 881 F.2d 832, 834 (9th Cir. 1989), *cert. denied* 493 U.S. 1070 (1990).

Petition for Rehearing

Petitioners sought rehearing and suggested rehearing *en banc*. While the petition and suggestion were pending, the Eighth Circuit published its decision in *Chutich v. Touche Ross & Co.*, 960 F.2d 721 (8th Cir. 1992) holding federal courts lack the power to imply a private right of contribution in section 10(b) of the Exchange Act and Rule 10b-5. Petitioners called the Ninth Circuit's *en banc* attention to the Eighth Circuit's decision and asked the Ninth Circuit to overrule *Smith v. Mulvaney*, resolving the circuit conflict. The Ninth Circuit denied the petition and rejected the suggestion of rehearing *en banc*.

REASONS FOR GRANTING THE WRIT

I.

THE NINTH CIRCUIT'S DECISION PERPETUATES AN EXPLICIT CONFLICT BETWEEN THE CIRCUIT COURTS

The Ninth Circuit has been a leading court endorsing creation of an implied right of contribution under section 10(b) and Rule 10b-5. *See Smith v. Mulvaney*, 827 F.2d 558, 560 (9th Cir. 1987). This case reaffirms the Ninth Circuit's dubious leadership. Although the Ninth Circuit is not alone, support for its position is eroding.

The initial circuit level decision implying a right of contribution was a *per curiam* opinion of the Second Circuit. *Globus, Inc. v. Law Research Service, Inc.*, 318 F.Supp. 955, 958, (S.D.N.Y. 1970), *aff'd*, 442 F.2d 1346 (2d Cir. 1970); *cert. denied*, 404 U.S. 941 (1971). Later in the decade,

the Seventh Circuit joined the Second. *Heizer Corp. v. Ross*, 601 F.2d 330, 331-34 (7th Cir. 1979). For several years, the lower federal courts tended to treat the existence of an implied right of contribution as settled.

In 1981, this Court held the federal courts have the power to recognize a right of contribution in only two circumstances: (1) "through the affirmative creation of a right of action by Congress, either expressly or by clear implication;" or (2) "through the power of federal courts to fashion a federal common law of contribution." *Texas Industries, Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 638 (1981).

The Seventh Circuit disavowed *Heizer* after considering this Court's *Texas Industries* analysis of the limits of federal judicial power. *King v. Gibbs*, 876 F.2d 1275, 1280 (7th Cir. 1989). Although *King v. Gibbs* holds federal courts lack power to imply a right of indemnity, the Seventh Circuit's reasoning and disavowal of *Heizer* created the first conflict of a court of appeals' decision with *Globus v. Law Research* and *Smith v. Mulvaney*.

Recently the Eighth Circuit explicitly held federal courts lack power to create a right of action for contribution under section 10(b). *Chutich v. Touche Ross & Co.*, 960 F.2d 721, 723-24 (8th Cir. 1992). In *Chutich*, the Eighth Circuit followed *Texas Industries*, agreed with *King* and criticized both *Smith v. Mulvaney* and a Second Circuit decision that followed *Globus* without considering the effect of *Texas Industries*.[2]

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[2] The criticized Second Circuit decision is *Sirota v. Solitron Devices, Inc.*, 673 F.2d 566, 588 (2d Cir. 1982), *cert. denied* 459 U.S. 838 (1982), *cert. denied*, 459 U.S. 908 (1982).

Other courts, applying *Texas Industries*, are recognizing they lack the power to imply a right of contribution in section 10(b). *In re Professional Financial Management, Ltd.*, 683 F.Supp. 1283, 1285-87 (D. Minn. 1988); *Robin v. Doctors Officenters Corp.*, 730 F.Supp. 122, 124-25 (N.D.Ill. 1989); *see also Baker, Watts & Co. v. Miles & Stockbridge*, 876 F.2d 1101, 1102-04 (4th Cir. 1989) (holding no right to contribution may be implied in section 12(2) of the Securities Act of 1933) (*en banc*), *reh'g denied* 1989 U.S.App. Lexis 13457 (4th Cir. 1989).

The conflict between the circuits requires this Court's attention. Securities claims are transitory causes of action, and jurisdiction exists nationwide. The huge sums at stake in securities cases encourage forum shopping. The conflict assures that substantial rights will depend entirely upon a suit's venue.

II.

THE NINTH CIRCUIT IGNORES THIS COURT'S VIEWS OF FEDERAL JUDICIAL POWER WHEN IT IMPLIES A RIGHT OF CONTRIBUTION IN SECTION 10(b)

The Ninth Circuit wrongly decided both *Smith v. Mulvaney* and this case. The Ninth Circuit failed to apply *Texas Industries*. *Texas Industries* requires federal courts not to create a private right of contribution in section 10(b) and Rule 10b-5.

There is no "affirmative creation of a right of action" for contribution in section 10(b). The section lacks any

express civil remedy. The section also lacks a "clear implication" of a right of contribution. Nothing in the comprehensive 1933 and 1934 securities legislation or its history suggests Congress intended to protect defendants in securities litigation. To the contrary, section 10(b) itself speaks of protection of investors and the public. Where Congress did intend to protect particular defendants, it created an express right of contribution; of the seven express civil remedies, exactly three are accompanied by express contribution rights. Section 11(f) of the Securities Act of 1933, 15 U.S.C. § 77k(f); Section 9(e) of the Exchange Act, 15 U.S.C. § 78i(e); Section 18(b) of the Exchange Act, 15 U.S.C. § 78r(b). Congress did not affirmatively create a right of contribution in section 10(b).

Federal courts lack authority to create a federal common law of contribution among defendants in section 10(b) cases. A federal rule of decision is not needed to protect uniquely federal interests. *Texas Industries*, 451 U.S. at 640. Contribution among alleged securities law violators does not involve "the rights and obligations of the United States, interstate and international disputes implicating the conflicting rights of States or our relations with foreign nations, [or] admiralty." *Texas Industries*, 451 U.S. at 641. Therefore contribution does not affect uniquely federal interests, and federal courts need not create federal common law. Further, the Exchange Act lacks any general charter for federal courts to develop a federal common law of securities regulation. *See Texas Industries*, 451 U.S. at 642-43. Creating a claim for contribution expands federal judicial power far beyond defining the limits of a fraud victim's implied claim under

section 10(b) and invents a new cause of action for persons outside the scope of those intended to be benefitted by either section 10(b) or the fraud victim's implied right of action.

III.

THE NINTH CIRCUIT'S DECISION FORMS A PART OF A DERIVATIVE FEDERAL COMMON LAW JURISPRUDENCE WHICH ILLUSTRATES WHY COURTS SHOULD NOT HAVE CREATED AN IMPLIED RIGHT OF CONTRIBUTION

Circuits recognizing an implied right of contribution are infected with a secondary jurisprudence of "contribution bars" and the rights of settling and non-settling defendants. This secondary jurisprudence contains its own unresolved circuit-level conflicts and impairs courts' management of complex securities cases. The decisions attempting to solve the problems caused by creating the right of contribution illustrate why courts should not have created such a right.

The secondary jurisprudence exists because, as one District Judge eloquently stated:

> Anyone foolish enough to settle without barring contribution is courting disaster.

In re Nucorp Energy Securities Litigation, 661 F.Supp. 1403, 1408 (S.D. Cal. 1987).

Defendants in complex securities litigation simply will not settle unless they are assured the settlement terminates entirely their involvement with the litigation. Lower federal courts have therefore developed a federal

common law of "contribution bars" or "settlement bars." *Singer v. Olympia Brewing Co.*, 878 F.2d 596, 599 (2d Cir. 1989), *cert. denied*, 493 U.S. 1024 (1990); *Franklin v. Kaypro Corp.*, 884 F.2d 1222, 1228-29 (9th Cir. 1989), *cert. denied*, 111 S.Ct. 232 (1990). This case is one of the Ninth Circuit's further elaborations of *Franklin*.

When they foreclose the contribution "rights" of some defendants, courts must consider how to protect those defendants from abusive or collusive settlements. A conflict exists between two inconsistent attempts to achieve fairness. In *Franklin*, the Ninth Circuit imposed the burden of determining fairness on the jury at trial. Under the *Franklin* rule, the jury must determine the relative fault of the settling defendants and the non-settling defendants; the non-settling defendants then are jointly liable for a percentage of the victims' total damage equal to their share of the relative fault. *Franklin*, 884 F.2d at 1231. In *Singer*, the Second Circuit required district courts to determine in a hearing at the time of the settlement whether the settlement is fair to the non-settling defendants; the amount of the settlement then is to be set off against from the plaintiffs' recovery from the non-settling defendants. *Singer*, 878 F.2d at 600.

Some courts have adopted the same view as *Franklin*. *United States Fidelity & Guaranty Co. v. Patriot's Point Development Authority*, 772 F.Supp. 1565 (D.S.C. 1990); *In re Sunrise Securities Litigation*, 698 F.Supp 1256 (E.D. Pa. 1988).

Some courts have adopted the approach of *Singer*. *In re Atlantic Financial Management, Inc. Securities Litigation*,

718 F.Supp. 1012 (D.Mass. 1988); *In re Terra-Drill Partnerships Securities Litigation*, 726 F.Supp. 655 (S.D. Tex. 1989); *Dalton v. Alston & Bird*, 741 F.Supp. 157 (S.D. Ill. 1990); *MFS Municipal Income Trust v. American Medical International Inc.*, 751 F.Supp. 279 (D.Mass. 1990).

Neither approach to settlement bars is satisfactory. The *Franklin* approach has nearly terminated partial settlements of securities class actions in the Ninth Circuit. *Franklin* intensly motivates non-settling defendants to pursue the "empty chair" defense and ironically forces plaintiffs to defend the cases of the persons with whom the plaintiffs settled. *Franklin* makes it impossible for plaintiffs to settle with highly culpable but financially strapped defendants. Further, *Franklin* burdens juries with extra decisions in cases notorious for their complexity. *Singer* forces trial judges to determine the fairness of settlements, often when the facts are insufficiently developed to provide confidence in the fairness of the determination. *Singer* generates additional burdens for both trial and appellate courts; if a settlement is reversed on appeal, the case management consequences are severe.

The conflict between the circuits regarding bar orders causes confusion and case management problems in the district courts. Indeed, the conflict itself has undone at least one settlement because neither the parties nor the trial judge could determine how to protect the rights of the non-settling defendants. *In re Jiffy Lube Securities Litigation*, 927 F.2d 155 (4th Cir. 1991).

The federal common law jurisprudence invented to control implied "rights" of contribution has become a malignant organism. It obstructs class action settlements

and complicates the duties of both judges and juries. The primary site of the malignancy is the authority creating the right of contribution. By excising the primary site, the Court will rid federal jurisprudence of the metastases as well.

CONCLUSION

For the foregoing reasons, including to resolve the explicit conflict between the Ninth Circuit's decision in this case and the decisions of the Eighth Circuit in *Chutich v. Touche Ross & Co.* and the Seventh Circuit in *King v. Gibbs*, a writ of certiorari should issue to review the judgment and opinion of the Court of Appeals for the Ninth Circuit.

Respectfully submitted,

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FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

EMPLOYERS INSURANCE OF WAUSAU; FEDERAL INSURANCE COMPANY,

Plaintiffs-Appellants,

v.

MUSICK, PEELER & GARRETT, A Partnership; LEONARD CASTRO, an Individual; ROBERT SCHUCHARD, an Individual; K.M.G. MAIN HURDMAN, A PARTNERSHIP; PEAT, MARWICK, MAIN & CO., a Partnership; J.H. COHN & CO., a Partnership; ED BACANI, an Individual; ROBERT TORKAR, an Individual; DOES 1 thru 100; and DOES 1 thru 300, Inclusive,

Defendants-Appellees.

No. 90-55791
D.C. No. CV-89-705-JLI
OPINION

Appeal from the United States District Court
for the Southern District of California
J. Lawrence Irving, District Judge, Presiding

Argued and Submitted
June 6, 1991 – Pasadena, California

Filed January 23, 1992

Before: Alfred T. Goodwin, Harry Pregerson and Arthur L. Alarcon, Circuit Judges.

Opinion by Judge Goodwin

COUNSEL

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OPINION

GOODWIN, Circuit Judge:

The securities fraud contribution question left open in *Franklin v. Kaypro Corp.*, 884 F.2d 1222 (9th Cir. 1989), *cert. denied sub nom., Franklin v. Peat Marwick Main & Co.*, 111 S. Ct. 232 (1990) is presented in this appeal by insurance carriers who are subrogated to the contribution rights of settling defendants (their insureds).

The plaintiffs seek recovery against nonparties now alleged to be culpable in the original public offering that resulted in the underlying litigation. *Kaypro* held that the district court could properly bar the nonsettling defendants from seeking contribution from the settling defendants, and held further that the nonsettling defendant's exposure should be limited to their actual percentage of liability based upon their culpability as determined by trial. *Kaypro* left open the contribution liability of nonparties who would have been defendants had they been sued by the original plaintiffs, but who were, for various reasons, not named as parties and thus were not participants in the settlement negotiations.

Employers Insurance of Wausau (Wausau) and Federal Insurance Co. (Federal), insurers of the settling defendants in a securities fraud class action, *In re Cousins Securities Litigation*, No. 84-1821-(IEG), appeal the dismissal of their action for contribution under federal law and for comparative equitable indemnity under state law against the defendants, persons who were the attorneys and accountants of the insureds in the public offering that gave rise to the class action suit.

Shareholders of Cousins Home Furnishings, Inc. filed the class action against insureds – Cousins, along with its holding company, certain of its officers and directors, and its two lead underwriters – alleging violations of federal securities law and California corporations law in connection with a public offering in 1983. The shareholders did not, however, sue, nor did insureds implead the attorneys and accountants involved in the underlying transaction. All defendants in the suit entered into a settlement agreement with the plaintiff class agreeing to pay plaintiff shareholders $13.5 million, an amount determined by a federal magistrate after a "good faith" hearing to "represent[ ] the settling defendants' fair or proper share of the total damages sought by the plaintiffs."

The settlement contained a general release from liability, including the release of potential claims by the plaintiff class against insureds' attorneys and accountants, even though they were not defendants. At the time of the agreement, the statute of limitations had already run on claims by the plaintiff class against the non-party lawyers and accountants. Although agreeing to the settlement, insureds expressly denied liability. Wausau and

Federal (the "Insurers") have paid their appropriate percentages of the settlement amount.

The Insurers now assert the right, as insureds' subrogees, to sue the attorneys and accountants. Insurers' complaint, which resembles the shareholders' complaint against insureds in the class action, alleges various misrepresentations that defendants caused insureds to make to investors about matters germane to the public offering, in violation of section 10(b) of the Securities Exchange Act of 1933 and Rule 10b-5 of the Securities Exchange Commission, 17 C.F.R. § 240.10b-5.

Holding that a settling defendant who has paid no more than its fair share of the total liability is not entitled to contribution under federal securities law, the district court dismissed the action without leave to amend for failure to state a claim upon which relief may be granted, pursuant to Fed. R. Civ. P. 12(b)(6). This court reviews the granting of a 12(b)(6) motion *de novo*. *Massey v. Inland Boatmen's Union of Pacific*, 886 F.2d 1188, 1189 (9th Cir. 1989). Because we find that the Insurers have stated a valid claim for contribution, we reverse.

No explicit right to contribution is provided for in section 10(b) of the Securities Exchange Act of 1933 or Rule 10b-5. We have recognized, however, that these provisions imply a right of contribution. *See Kaypro*, 884 F.2d at 1226; *Smith v. Mulvaney*, 827 F.2d 558, 561 (9th Cir. 1987).

Actions for contribution arise in many different procedural settings. For example, contribution may be sought by one defendant against other named defendants by a motion to the court, *see Globus, Inc. v. Law Research*

Service, Inc., 318 F.Supp. 955, 957 (S.D.N.Y. 1970), *aff'd*, 442 F.2d 1346 (2nd Cir.), *cert. denied sub nom., Law Research Service, Inc. v. Blair & Co.*, 404 U.S. 941 (1971). An individual seeking contribution is not limited, however, to the parties named by the plaintiff in the original suit. Contribution may be the [sic] sought through a third party action pursuant to Rule 14(a) of the Federal Rules of Civil Procedure. *See Tucker v. Arthur Andersen & Co.*, 646F.2d 721, 727 n.7 (2nd Cir. 1981); *Odette v. Shearson Hammill & Co., Inc.*, 394 F.Supp. 946, 958 (S.D.N.Y. 1975); *Leggett & Myers, Inc. v. Bloomfield*, 380 F.Supp. 1044, 1047 (S.D.N.Y. 1974).

While actions for contribution are frequently brought in the context of third party practice, it does not follow that third party procedure is the exclusive remedy. The right of contribution is substantive in nature. "Rule 14, like all of the Federal Rules of Civil Procedure, is purely procedural. It does not create or modify any substantive rights, such as the right to indemnification or contribution." 3 Moore's Fed. Prac., ¶ 14.03[1]. Thus, a claim for contribution may be maintained in a separate action. *Heizer Corp. v. Ross*, 601 F.2d 330, 334 (7th Cir. 1979). *See also* Restatement (Second) of Torts § 886A(2) comment i (1979) ("A separate action for contribution is also available, particularly against a tortfeasor who was not a party to the original action.").

The provisions of the securities laws that explicitly provide for contribution envision the possibility of such claims being brought as separate causes of action. Contribution is not limited to parties involved in the original suit. Section 78r(b), for example, provides:

> Every person who becomes liable to make payment under this section may recover contribution as in cases of contract from any person who, *if joined in the original suit*, would have been liable to make the same payment.

15 U.S.C. § 78r(b) (emphasis added). Actions for contribution may be brought, as in this case, in a separate proceeding.

The law of contribution is intricate, but the basic principle is easy to state:

> Typically, a right to contribution is recognized when two or more persons are liable to the same plaintiff for the same injury and one of the joint tortfeasors has paid more than his fair share of the common liability. Recognition of the right reflects the view that when two or more persons share responsibility for a wrong, it is inequitable to require one to pay the entire cost of reparation, and it is sound policy to deter all wrongdoers by reducing the likelihood that any will entirely escape liability.

Northwest Airlines, Inc. v. Transport Workers Union, 451 U.S. 77, 87-88 (1981) (footnotes omitted).

The defendants argue that an action for contribution exists only when an individual has paid more than her "fair share"of the common liability. Since the court in *Cousins* found that the settlement represented the insureds "fair and proper share of the total damages sought against them in the action," the defendants contend that the present action was properly dismissed.

The problem with this argument is that it fails to recognize that the meaning of the term "fair share"

depends upon the context in which it is used. The concept of fairness is inherently relational. There are three distinct relationships involved in the present case, each of which engenders a separate standard to assess the fairness of the *Cousins* settlement: (i) the relationship between individual *Cousins* defendants and the plaintiff class, (ii) the relationship between the *Cousins* defendants, "inter se," and (iii) the relationship between the *Cousins* defendants and joint tortfeasors who were not party to the suit.

Given that all tortfeasors are jointly and severally liable for the damages suffered by the plaintiff class, if only one of them were sued, it would be "fair" for that individual to be required to pay plaintiffs the full amount of the damages. The total sum of the damages would be that defendant's "fair share." When a number of joint tortfeasors are named as defendants, then the "fair share" of individual defendants is determined by their relative culpability. *Smith v. Mulvaney*, 827 F.2d at 561. "Relative" in this context is defined "interse," in reference to the other defendants involved to the suit. The failure to join all culpable actors has the obvious effect of inflating the relative culpability of the parties who are joined.

In approving the settlement agreement, the court in *Cousins* had to make two assessments. First, the court had to determine whether the total amount of the settlement bore a reasonable relationship to the damage suffered by the plaintiff class, discounting for factors such as the cost and uncertainty involved in litigating the dispute. Second, the court had to determine whether the amount paid

by each individual defendant was "fair" given their culpability *relative to the other defendants involved in the litigation*. It was in this context that the court determined that the settlement agreement represented the defendants' "fair and proper share of the total damages."

An action for contribution is concerned with the third type of fairness, that of the individual tortfeasor relative to all others jointly liable for the injury. If an individual pays more that [sic] her "fair share of the common liability," then an action for contribution will lie. *Northwest Airlines*, 451 U.S. at 88. It is axiomatic that a defendant may pay her fair share relative to other parties in the suit and yet pay more than her fair share relative to the universe of all joint tortfeaasors.[1] If a party can establish these facts, then she has stated a cause of action upon which relief may be granted and can successfully avoid a 12(b)(6) motion.

The defendants argue that the "good faith" approval of the settlement agreement by the court in *Cousins* should bar the present action. They misread the reach of

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[1] This is not to say that an action for contribution will always lie against non-party joint tortfeasors when named defendants negotiate a settlement agreement. The amount of damages in the settlement agreement is frequently discounted to reflect the cost and uncertainty associated with litigation. In determining whether or not an individual has paid more than her "fair share" for the purposes of contribution, the total amount of common liability is not discounted. If the discounting of the settlement amount is substantial, then a party to the settlement agreement may pay less than her "fair share" for purposes of contribution despite the fact that her relative culpability for purposes of the settlement agreement is inflated because all culpable parties were not joined.

the good faith hearing.[2] In the area of securities litigation, this issue is governed by federal common law. *See Kaypro*, 884 F.2d at 1228.

Kaypro involved a partial settlement agreement containing an express bar against suits for contribution by nonsettling defendants against settling defendants in a section 10(b) securities fraud suit. The court upheld the bar and outlined a scheme that protected the interests of all parties while, at the same time, encouraging settlement.

> This scheme contemplates a partial settlement approved by the district court under Rule 23. Non-settling defendants are then barred from further rights of contribution from the settling defendants. At trial, the jury is asked not only to determine the total damage amount, but also the percentage of culpability of each of the non-settling defendants as well as that of the settling defendants. Nonsettling defendants as a whole will then be required to pay the percentage of the total amount for which they are responsible. The nonsettling defendants will be jointly and severally liable for that percentage, and will continue to have rights of contribution against one another.

884 F.2d at 1231 (footnote omitted).

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[2] While in the context of federal maritime law and not securities law, *Miller v. Christopher*, 887 F.2d 902, 903-07 (9th Cir. 1989) provides an extensive discussion of the general issues invoked by a good faith settlement bar to actions for contribution.

While *Kaypro* goes far in clarifying the rights of settling and nonsettling defendants in the context of a partial settlement agreement, it provides little direct guidance as to the rights of settling defendants with respect to nonparties.[3] We hold that a settlement agreement cannot be relied upon to bar subsequent actions for contribution by settling defendants against individuals who were not party to the original suit. The logic of allowing defendants to enter into partial settlement agreements, paying damage awards that reflect their culpability relative to other parties in the suit and obtaining protection against subsequent claims for contribution by non-settling defendants, does not bar claims by settling defendants against nonparties.

This holding promotes the three goals identified by the court in *Kaypro*. First, allowing suits against nonparties satisfies the "statutory goal of punishing each wrongdoer." 884 F.2d at 1231. To hold otherwise would immunize an entire category of joint tortfeasors from

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[3] Two other Ninth Circuit cases involve the effect of settlement on subsequent actions for contribution in securities cases. Neither case considers the effect of settlement on nonparties. After *Kaypro, Laventhol, Krekstein, Horwath, & Horwath v. Horwitch*, 637 F.2d 672, 675 (9th Cir. 1980), *cert. denied, Frank v. United States Trust Co.*, 452 U.S. 963 (1981), should be read for the proposition that a settlement, not reflecting the settling defendants' proper share of the damages, will not bar subsequent actions for contribution by nonsettling defendants. *Smith v. Mulvaney* held that summary judgement in an action for contribution by a non-settling defendant against settling defendants was inappropriate if there exists a genuine issue of material fact as to whether the settling defendants paid their "proper share of damages." 887 F.2d at 562.

responsibility and thwart the deterent objective of the laws regulating securities exchanges. Second, allowing suits against nonparties satisfies the "equitable goal of limiting liability to relative culpability." *Id.* Individuals are held accountable for that portion of the common liability for which they are culpable relative to the universe of all joint tortfeasors, and not simply relative to those individuals named by the plaintiff in the original action. Finally, allowing suits against nonparties satisfies the "policy goal of encouraging settlement." *Id.* Named defendants will be more likely to settle if they are not penalized for doing so by being prohibited from pursuing subsequent claims for contribution against nonparties.

The defendants argue that allowing suits against nonparties will prevent litigation from ever being quieted. There is an important difference between quieting existing litigation and barring legitimate and distinct causes of action. The settlement agreement brought to an end the dispute between the *Cousins* plaintiff class and the *Cousins* defendants. The settlement also quieted potential "inter se" claims between the *Cousins* defendants.

There is something inherently "dis-quieting" about contribution claims. These actions threaten to reopen many of the same issues raised in the original controversy. It is also undeniable that, from the standpoint of judicial economy, it is more desirable for all claims to be resolved in a single proceeding. These costs, however, were deemed acceptable in the context of securities law when Congress explicitly provided for contribution, 15

U.S.C. §§ 77k, 78i, and 78r, and implied a right of contribution in section 10(b), a right that can be pursued in a separate cause of action.

Our ruling will not cause an endless stream of contribution claims. The doctrine of contribution contains two important internal checks. No cause of action will lie unless a party has paid more than her share of the total amount of common liability, a sum that is not necessarily equivalent to the amount of the settlement agreement.[4] Second, a party becomes immune from any action for contribution once she has paid her share of the damages.

In the district court, the defendants argued a number of other rationales in support of the 12(b)(6) motion, arguments which have also been briefed on appeal. The district court did not base its decision on these grounds. Moreover, we find the arguments to be without merit. The claims of judicial and collateral estoppel relating to representations and findings that the *Cousins* settlement constituted the defendants "fair share" of the total damages are misguided for the same reason that an action of contribution exists: "fairness" in the *Cousins* context was limited to an "inter se" assessment.

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[4] Economic incentives continue to favor impleading a party in a third party action rather than seeking contribution in a separate suit. Besides the additional costs involved in a separate action, the impled party must pay her relative share of the total settlement amount, whereas damages in a separate suit are limited to the amount the settling defendant paid in excess of her share of the total amount of actual damages. The later sum will always be a smaller amount if the settlement amount is discounted in any fashion.

Defendants claim that no action for contribution can exist because, given insureds position in *Cousins*, they cannot be *joint* tortfeasors. This argument fails to recognize that, in the present action, the Insurers contend that at least some of the insureds were wrongdoers. Moreover, the primary authority relied upon by the defendants, *In re Agent Orange Product Liability Litigation*, 818 F.2d 204, (2nd Cir. 1987), is distinguishable. In that case the appellants maintained, *in the action for contribution*, that Agent Orange caused no harm. The court indicated that the situation would be different if the "appellants would abandon their 'no-fault' stance." *Id.* at 207.

Finally, the defendants assert that the doctrine of "superior equities" should bar the Insurers' claim for contribution. Our decision is guided by federal securities statutes and the federal common law. *Kaypro*, 884 F.2d at 1228. The defendants can cite no case supporting the existence of a doctrine of "superior equities" in this setting, nor do we find the reasoning persuasive enough to import the requirement. The long-standing bar against claims for indemnification in securities cases, *see Laventhol*, 637 F.2d at 676; *Heizer Corp.*, 601 F.2d at 334, and the rule that damages in actions for contribution are determined by a standard of relative culpability, *see Smith v. Mulvaney*, 827 F.2d at 561, are sufficient to protect the equitable interests of the parties.

The plaintiffs have successfully stated a claim upon which relief may be granted. The 12(b)(6) motion should have been denied.

REVERSED AND REMANDED

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

EMPLOYERS INSURANCE OF WAUSAU and FEDERAL INSURANCE COMPANY, Plaintiffs, v. MUSICK, PEELER & GARRETT, LEONARD CASTRO, ROBERT SCHUCHARD, KMG MAIN HURDMAN, PEAT, MARWICK, MAIN & CO., J. H. COHN & CO., ED BACANI, ROBERT TORKAR, DOES 1 through 100, and ROES 1 through 300, Inclusive, Defendants.	No. 89-0705-JLI(BTM) MEMORANDUM DECISION AND ORDER (Filed Apr. 10, 1990)

The defendants' motions for a contempt order, dismissal or disqualification of the plaintiffs' counsel, dismissal pursuant to Federal Rule of Civil Procedure 12(b)(6), and the striking of "Doe" and "Roe" defendants came on for hearing on April 2, 1990, at 10:30 a.m. before the Honorable J. Lawrence Irving, District Judge. Lawrence Nagler, Larry Goldberg and Harry Rebhuhn appeared on behalf of the plaintiffs. William Reifman appeared for the defendants Peat Marwick Main & Co. ("Peat") and K.M.G. Main Hurdman ("Main"), and Alvin Stein appeared on behalf of the defendants J. H. Cohn &

Co. ("Cohn"), Ed Bacani and Robert Torkor. Charles Bird appeared for the defendants Musick Peeler & Garrett ("Musick"), Leonard Castro and Robert Schuchard.

Having considered all pleadings, declarations and the written and oral arguments of counsel and law in support thereof, the Court hereby: (1) grants the defendants' motion to dismiss under Federal Rule of Civil Procedure 12(b)(6); (2) denies defendants' motion for a contempt order, dismissal or disqualification of the plaintiffs' counsel; and (3) grants the defendants' motion to strike the "Doe" and "Roe" defendants.

FACTS

This case arises as a direct result of the settlement of *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG) ("*Cousins*"). *Cousins* was a large class action in which shareholders of the Cousins Corporation ("Cousins") charged Cousins, the holding company of Cousins, various Cousins officers and directors, and two lead underwriters with violation of the federal securities laws through the omission of material facts in connection with the sale of stock during a December 1983, public offering ("Cousins public offering"). The case ultimately settled, and the defendants and their insurance carriers agreed to pay the plaintiffs $13,500,000.

Prior to settlement, United States Magistrate Irma E. Gonzalez held two hearings in order to determine whether the proposed settlement had been made in good faith. The purpose of these hearings, as enumerated by the *Cousins* parties, was to determine whether the settling defendants were going to pay "a fair, reasonable and

adequate proportion of the total damages sought based upon the claims asserted by the Settlement Class Members. . . . " Stipulation of Settlement, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 14 (June 17, 1988) (Exhibit 4 to the Request that Court Take Judicial Notice of the defendants Peat and Main). At the second, final hearing, magistrate Gonzalez held that "the settlement set forth in the stipulation represents the settling defendants' fair or proper share of the total damages sought by the plaintiffs for alleged violations of Federal Securities laws. . . . " Transcript of Good Faith Hearing Re Settlement, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 5 (August 29, 1988).

The plaintiffs to the instant case are Employers Insurance of Wausau ("Wausau") and Federal Insurance Company ("Federal"), the two carriers that insured most of the *Cousins* defendants. On behalf of their insureds, the plaintiffs have already paid a large portion of the *Cousins* settlement sum.

The plaintiffs believe that the defendant lawyers and accountants should be held partly responsible for the injuries allegedly suffered by the *Cousins* plaintiffs. They therefore have brought this suit for contribution and indemnity against: (1) Musick, the law firm that worked on the Cousins public offering; (2) Peat, an accounting firm involved with the Cousins public offering; (3) Main, another accounting firm involved with the Cousins public offering; (4) Cohn, another accounting firm involved with the Cousins public offering; (5) Leonard Castro and Robert Schuchard, two Musick partners; (6) Ed Bacani and Robert Torkar, two Cohn partners; and (7) various "Doe" and "Roe" defendants. The plaintiffs allege that

these the defendants are jointly and severally liable for any securities frauds perpetrated upon the *Cousins* plaintiffs.

The plaintiffs' first amended complaint, filed on July 18, 1989, seeks the following relief: (1) contribution by Musick and its partners under federal law for violations of Section 10(b) and Rule 10b-5 of the 1933 Federal Securities Exchange Act ("Exchange Act"); (2) equitable indemnity from Musick and its partners under state law for violations of Section 10(b) and Rule 10b-5 of the Exchange Act; (3) contribution by Peat, Main, Cohn and the Cohn partners under state law for violations of Section 10(b) and Rule 10b-5 of the Exchange Act; (4) equitable indemnity from Peat, Main, Cohn, and the Cohn partners under state law for violations of Section 10(b) and Rule 10b-5 of the Exchange Act; (5) contribution by Peat, Main, Cohn and the Cohn partners under federal law for violations of Section 11 of the 1934 Federal Securities Act; (6) equitable indemnity from Peat, Main, Cohn and the Cohn partners under state law for violations of Section 11 of the 1934 Federal Securities Act; (7) equitable indemnity from Peat, Main, Cohn and the Cohn partners under state law for violations of Sections 25401, 25501, 25504.1 and 25504.2 of the California Corporations Code; (8) equitable indemnity from Musick and its partners under state law for negligence; and (9) equitable indemnity from Peat, Main, Cohn and the Cohn partners under state law for negligence.

In response to the complaint, the defendants have filed the following motions: (1) motion to dismiss under Federal Rule of Civil Procedure 12(b)(6); (2) motion for

contempt order, dismissal or disqualification of the plaintiffs' counsel; and (3) motion to strike the "Doe" and "Roe" defendants.

DISCUSSION

1. Motion to Dismiss For Failure to State A Cause of Action Upon Which Relief Can Be Granted

The defendants argue that dismissal of this suit is warranted under Rule 12(b)(6) of the Federal Rules of Civil Procedure because under *Franklin v. Kaypro*, 884 F.2d 1222 (9th Cir. 1989), the plaintiffs have failed to state a cause of action upon which relief can be granted. F.R.Civ.P. 12(b)(6). In *Kaypro*, a Ninth Circuit panel[1] determined that under the federal common law the contribution rights of non-settling defendants against settling defendants in federal securities actions are cut off once a court determines that the settlement has been made in good faith. *Id*. The court held that during trial of such cases the jury should be asked to determine the total dollar amount of damages as well as the percentage of culpability of all settling and non-settling defendants. *Id*. at 1231. Non-settling defendants as a whole are then required to pay the percentage of the total amount for which they are found responsible. *Id*.

The *Kaypro* court follows a long line of Ninth Circuit cases which emphasize that equity must not be sacrificed by the right to contribution; no defendant should ever be

[1] The panel was made up of Judges Farris, Beezer and Ferguson.

held responsible for more than his or her "fair share" of the total liability. In *Smith v. Mulvaney*, 827 F.2d 558, 561 (9th Cir. 1987), the Ninth Circuit found that "[c]ontribution is an equitable doctrine. To apportion damages without regard to fault reduces, to an extent, the equity which the doctrine was intended to provide."

The *Kaypro* court specifically reiterates this concern as it relates to securities class actions. It states: "Although we do not lose sight of the fact that we are speaking of equities between wrongdoers, we decline to back away from our goal of equity." *Kaypro*, 884 F.2d at 1231. Thus, under *Kaypro*, once a defendant has settled, his or her share of the liability has been satisfied, and he or she is protected from suits for contribution. *Id*. Alternatively, he or she cannot seek contribution from non-settling defendants if he or she settles for a sum larger than the ultimate trial verdict. *Id*. at 1231-32.

The defendants argue that it follows, *a fortiori*, that settling defendants who have paid their "fair share" should not be able to enjoy contribution from non-parties. Such a reading of *Kaypro* is consistent with prior authority. The federal courts in general have consistently held that a party has a right to contribution only when he or she has paid more than his or her fair share of the liability. In *Northwest Airlines, Inc. v. Transport Workers of America*, 451 U.S. 77, 87-88 (1981), the Supreme Court held that a right to contribution is recognized when two or more persons "are liable to the same plaintiff for the same injury and one of the joint tortfeasors has paid more than his fair share of the common liability." A court in the Eastern District of California expanded upon this holding by stating that the right of contribution may be enforced

only if one of two or more joint wrongdoers has paid more than his or her pro rata share of the liability. *Harrison v. Sheats*, 608 F. Supp. 502, 505 (E. D. Cal. 1985).

To refute this conclusion, the plaintiffs rely upon *Dube v. Pittsburgh-Corning Corp.*, 1988 WL 64733 (U.S.D.C., D. Me. 1988), *aff'd in part and rev'd in part*, 870 F.2d 890 (1st Cir. 1989), in which the district court of Maine permitted four settling defendants to sue a non-party for contribution. *Dube*, however, is not inconsistent with the defendants' argument. In *Dube*, four settling asbestos manufacturers sued the United States, a non-party, for contribution. In an unpublished opinion, the *Dube* court applied Maine law and held that the settling defendants had a right to contribution because the United States was partially responsible for the damages incurred. *Id.* at 9. In making this determination, the *Dube* court decided the relative culpability of the four settling defendants and of the United States, a determination that, unlike the situations in *Northwest* and *Harrison*, had not previously been made. Deciding that the settling defendants were only responsible for two-thirds of the settlement amount, the court, like those in *Northwest* and *Harrison*, required them to pay only this "fair share." *Id.*

In support of their assertion that contribution is appropriate, the plaintiffs also rely on a number of California cases. Yet the plaintiffs' reliance on these cases is misplaced; the cases, which are non-binding authority, concur with defendants' argument. For example, in *American Bankers Insurance Co. v. Avco-Lycoming Division*, 97 Cal. App. 3d 732, 159 Cal. Rptr. 70 (1979), the California Court of Appeals held that a settling defendant who agreed to pay the full amount of a plaintiff's claim had a

right to contribution from a co-defendant who had been dismissed from the case as part of the settlement. This is exactly the situation in *Dube*. The settling defendant had assumed total responsibility for the injuries the plaintiff suffered, thereby paying *more* than his pro rata share of liability. *Id.* Under the "fair share" doctrine, the settling defendant was entitled to sue his co-defendants for contribution.

Thus, the question in the instant case is: was the amount for which the *Cousins* parties settled deemed to be the settling defendants' "fair share" of the total liability or was it meant to compensate the *Cousins* plaintiffs for all the injuries they incurred? In reviewing the documents relating to the *Cousins* good faith settlement hearing, it is clear that all the *Cousins* parties understood and the *Cousins* court held that the $13,500,000 for which the plaintiffs settled was meant to encompass only the "fair share" of the settling defendants' liability. In their motion for a determination of good faith settlement, the *Cousins* defendants asked the court to determine that the settlement with the plaintiffs was made in good faith and that the defendants were "paying directly or by their insurers a *fair and proper share* of the total damages sought *against them* in the action." Defendants' Notice of Motion and Motion for a Determination of Good Faith Settlement, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 2 (July 11, 1988) (emphasis added). In the stipulated settlement, the parties agreed that the settling defendants were "paying, directly or by their Insurers, a fair, reasonable and adequate proportion of the total damages sought based upon the claims asserted by the Settlement Class Members. . . . " Stipulation of Settlement, *In Re Cousins*

Securities Litigation, No. 84-1821-B(IEG), at 14 (June 17, 1988). In a declaration in support of a *Cousins* defendant's motion for a good faith settlement determination, David Stern, counsel to Cousins, asserted that the settling defendants were paying, directly or by their insurers, "a fair and proper share of the total damages sought against them in the action." Declaration of David B. Stern in Support of Defendant's Motion for Good Faith Settlement Determination, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 1 (July 11, 1988). Finally, at the last good faith settlement hearing, Magistrate Gonzalez specifically stated: "I find that the settlement set forth in the stipulation represents the settling Defendants' *fair or proper share* of the total damages sought by the Plaintiffs for alleged violations of the Federal securities laws and, when viewed in the totality of the circumstances, the settlement of the Federal causes of action is fundamentally fair and equitable." Transcript of Good Faith Hearing Re Settlement, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 5 (August 29, 1988) (emphasis added).

In opposition, the plaintiffs point to the following statement made by Mr. Bertrand Cooper, attorney for one of the defendants, at the first good faith settlement hearing:

> [T]here is a possibility that some or all of the carriers, insurance carriers, may wish to assert rights over, or possible rights over, that their assured have against third parties, I think notably accountants and/or lawyers; that the releases, to the extent releases are given by insureds to insurers, should be crafted in such a way so that if those accountant and lawyers against whom claims over are asserted, assert

> claims back against the insureds who are settling here, those insureds are not giving up any rights they may have under those insurance policies by virtue of any release in this action.

Transcript of Good Faith Hearing, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 19 (March 11, 1988). The plaintiffs argue that this language proves that the *Cousins* court specifically contemplated and approved the instant suit. They argue that this Court is accordingly required to uphold the terms of the *Cousins* settlement, as determined by Magistrate Gonzalez.

The plaintiffs read too much into this language. Although Mr. Cooper's statements indicate that the *Cousins* court was advised by one attorney of the possibility of a contribution suit against the lawyers and accountants who worked on the Cousins public offering, at no point did the *Cousins* court express its approval of such a cause of action. Since the court passed on the statements without comment, Mr. Cooper's words do not bind this Court to deny the defendants' motion to dismiss.

The Court is further influenced by another concern enunciated in *Kaypro* – that of encouraging settlement. The *Kaypro* court explicitly recognized "an overriding public interest in settling and quieting litigation . . . in class action suits. . . . " *Franklin v. Kaypro Corp.*, 884 F.2d 1222, 1229 (9th Cir. 1989) (*citing Von Bronkhorst v. Safeco Corp.*, 529 F.2d 943, 950 (9th Cir. 1976). Indeed, prohibiting the satisfaction of contribution rights prior to trial effectively eliminates partial settlements because "[a]nyone foolish enough to settle without barring contribution is courting disaster. They are allowing the total

damages from which their ultimate share will be derived to be determined in a trial where they are not even represented." *In Re Nucorp Securities Litigation*, 661 F. Supp. 1403, 1408 (S. D. Cal. 1987).

The Court's denial of the defendants' motion to dismiss would result in just such a disaster. As Mr. Stein indicated at oral argument, his clients will feel compelled to implead the *Cousins* plaintiffs if this case proceeds. Indeed, Mr. Nagler, the plaintiffs' counsel, has admitted that pursuit of this case might require him to put on a case against the very insureds whose interests his clients are supposed to protect. The result would be as if *Cousins* had never settled; all issues relating to that action would still have to be resolved in a very long and expensive trial. Given this Court's interest in promoting settlement[2] and for the other reasons stated, the defendants' motion to dismiss is hereby granted.

2. Motion for Contempt Order, Dismissal or Disqualification

The defendants argue that the plaintiffs are in contempt of court because, in framing their complaint, they

[2] Settlements are desirable, not just because trials are costly but because they allow parties to " 'manage their own disputes' and avoid the uncertainties and limitations of the winner-take-all, imposed decisions that courts make in fully litigated cases. Settlement also offers privacy to litigants and enables them to consider opportunities for resolutions that would not be available in a trial judgment." D. Provine, *Settlement Strategies for Federal District Judges*, at 1-2 (1986).

relied on protected information acquired through discovery of the *Cousins* case. The defendants believe that two protective orders issued by Judge Rudi M. Brewster expressly prohibit the *Cousins* parties from using such information for any purpose other than preparation for the *Cousins* trial.

Extensive discovery took place in preparation for the *Cousins* trial. During the course of discovery, Judge Brewster, the judge who presided over *Cousins*, entered two protective orders to which each *Cousins* party stipulated. The first protective order ("global order") was issued on January 23, 1985. The second protective order was issued at the request of Main, an interested non-party, and was filed on August 6, 1985. The global order contained language providing that: "All information produced or exchanged in the course of this case shall be used solely for the purpose of this case only and shall not be made available to persons other than qualified persons. . . . " Stipulation and Protective Order, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 2 (Jan. 23, 1985) (Exhibit 2 to the Request that Court Take Judicial Notice of the defendants Peat and Main). In addition, the global order instituted a procedure whereby certain documents could be labeled "confidential"; all "confidential" materials were to be filed under seal. *Id.* at 6. The second order stated: "All documents produced and deposition testimony given by Main Hurdman in this action are deemed to be confidential, shall be used solely for the purpose of this case and shall not be made available. . . . " Stipulation and Protective Order, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 2 (August 6, 1985)

(Exhibit 3 to the Request that Court Take Judicial Notice of the defendants Peat and Main).

Although the plaintiffs' attorneys admit that they have based their complaint upon information acquired during discovery of *Cousins*, they correctly argue that this Court does not have the power to order them in contempt. Here the plaintiffs are charged with violating two orders issued by Judge Brewster. It has long been established that a party who violates a court order may only be held in contempt by the court that issued the order. *In Re Debs*, 158 U.S. 564, 594-95 (1895). Accordingly, only Judge Brewster has the power to order these plaintiffs in contempt. *Id.; see Lubrizol Corp. v. Exxon Corp.*, 871 F.2d 1279 (5th Cir. 1989) ("We are aware of no basis upon which a district court may assert subject matter jurisdiction over violations of orders issued in other federal courts."). Thus, this Court denies the defendants' request for a contempt order.

Nor is dismissal of the complaint appropriate. Despite the defendants' assertions to the contrary, it is unclear whether the defendants violated the protective orders issued by the *Cousins* court. Both protective orders prohibit the provision of information to "qualified persons," or persons in direct competition with one or more of the *Cousins* parties. Stipulation and Protective Order, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 2-3 (Jan. 23, 1985); Stipulation and Protective Order, *In Re Cousins Securities Litigation*, No. 84-1821-B(IEG), at 2-4 (August 6, 1985). Neither contemplates nor expressly disallows the filing of a law suit based on such information. It is therefore unclear whether the orders apply to such a situation. *See* Declaration of Larry Goldberg, at 2-3

(Exhibit 9 to The plaintiffs' Request that Court Take Judicial Notice). Accordingly, this Court cannot conclude that the plaintiffs have exercised blatant disregard for Judge Brewster's orders, and this Court denies the defendants' motion to dismiss. *See North American Watch Corp. v. Princess Ermine Jewels*, 786 F.2d 1447, 1451 (9th Cir. 1986) (dismissal was warranted only in *extreme* case of refusal to abide by court's order).

The motion to disqualify the plaintiffs' counsel is also denied. As discussed above, it is unclear whether the plaintiffs violated the *Cousins* protective orders; both parties can point to language in the orders that supports their interpretations of the court's intent. Declaration of Larry Goldberg, at 2-3 (Exhibit 9 to the Plaintiffs' Request that Court Take Judicial Notice). Yet even if it is determined that the plaintiffs did violate the protective orders,[3] the plaintiffs counsel should not be prevented from pursuing this case. When there is a genuine misunderstanding as to the meaning of a protective order, disqualification is inappropriate. *See Syufy Enterprises v. Columbia Pictures Industries, Inc.*, 1978-2 Trade Cases P. 62,170 1978 WL 1372 (D. Utah 1978).

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[3] This issue is specifically reserved for resolution by Judge Brewster. As the judge who issued the two orders in question, his court is the one most qualified to decide whether a violation has occurred.

3. Motion to Strike the "Doe" and "Roe" Defendants

Finally, the defendants argue that since the Federal Rules of Civil Procedure make no provision for the naming of "Doe" and "Roe" defendants, the "Doe" and "Roe" defendants named in the instant case should be stricken from the complaint. As support for this proposition, they cite *Lubin v. Sybedon Corp.*, 688 F. Supp. 1425 (S. D. Cal. 1988), in which the court held that "Doe" defendants may not be named in federal securities actions. Other Ninth Circuit opinions support the *Lubin* decision. *See, e.g., Fifth Associates v. Prudential Insurance Co. of America*, 446 F.2d 1187, 1191 (9th Cir. 1970) (a suit naming "Doe" defendants may not be maintained in federal court).

In opposition to the defendants' motion to strike the "Doe" and "Roe" defendants, the plaintiffs argue that California law allows for the naming of "Doe" defendants, thereby "relating the complaint back" to the time of filing. California law, however, is irrelevant here; although the California "relation back" doctrine has been deemed substantive,[4] the rule as to naming "Doe" defendants is clearly procedural. Accordingly, Ninth Circuit authority on the naming of "Doe" defendants applies to this case. Under such authority, this Court hereby grants the defendants' motion to strike the "Doe" and "Roe" defendants.

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[4] *See Lindley v. General Electric Corp.*, 780 F.2d 797 (9th Cir. 1986).

CONCLUSION

1. The defendants' motion to dismiss for failure to state a cause of action is hereby granted. The Court finds that the plaintiffs who, on behalf of their insureds, have paid no more in settlement of *Cousins* than that which was their fair share of liability, are not entitled to sue the defendants for contribution, and allowing this action to go to trial would vitiate this Court's interest in encouraging settlement.

2. The defendants' motion for a contempt order, dismissal or disqualification is hereby denied. The Court finds that it does not have the authority to find the plaintiffs in contempt of court and that dismissal and disqualification are inappropriate because the plaintiffs have not exercised blatant disregard for the two *Cousins* protective orders.

3. The defendants' motion to strike the "Doe" and "Roe" defendants from the complaint is hereby granted. The Court finds that the naming of "Doe" and "Roe" defendants is not permitted in federal court.

IT IS SO ORDERED.

Dated: April 9, 1990

/s/ J. Lawrence Irving
J. LAWRENCE IRVING, JUDGE
UNITED STATES DISTRICT COURT

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UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

Employers Insurance of Wausau and Federal Insurance Company

v.

Musick, Petter & Garrett, Leonard Castro, Robert Schuchard, KMG Main Hurdman, Peat, Marwick, Main & CO et al

JUDGMENT IN A CIVIL CASE

(Filed Apr. 12, 1990)

CASE NUMBER: 89-0705-JLI(BTM)

_ **Jury Verdict.** This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.

X **Decision by Court.** This action came to trial or hearing before the Court. The issues have been tried or heard and a decision has been rendered.

IT IS ORDERED AND ADJUDGED that the defendants' motion to dismiss for failure to state a cause of action is hereby granted. The defendants' motion for a contempt order, dismissal or disqualification is hereby denied. The defendants' motion to strike the "Doe" and "Roe" defendants from the complaint is hereby granted .....

April 12, 1990
Date

WILLIAM W. LUDDY
Clerk

/s/ Mary Miramontes
(By) Deputy Clerk

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

EMPLOYERS INSURANCE OF WAUSAU; FEDERAL INSURANCE COMPANY Plaintiffs - Appellants, v. MUSICK, PELLER & GARRETT, a Partnership; LEONARD CASTRO, an Individual; ROBERT SCHUCHARD, an Individual; K.M.G. MAIN HURDMAN, a Partnership; PEAT, MARWICK, MAIN & CO., a Partnership; J.H. COHN & CO., a Partnership; ED BACANI, an Individual; ROBERT TORKAR, an Individual; DOES 1 thru 100; and DOES 1 thru 300, Inclusive, Defendants - Appellees.	No. 90-55791 D.C. No. CV-89-705-JLI O R D E R (Filed May 28, 1992)

Before: GOODWIN, PREGERSON, ALARCON, Circuit Judges.

The panel has voted unanimously to deny the petition for rehearing. Judges Pregerson and Alarcon have voted to reject the suggestion for rehearing en banc, and Judge Goodwin so recommends.

The full court has been advised of the suggestion for rehearing en banc and no active judge has requested a vote on whether to rehear the matter en banc. Fed. R. App. P. 35.

The petition for rehearing is DENIED and the suggestion for rehearing en banc is REJECTED.

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